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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
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In the Matter of	)	
	)	
Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket No. 92-266
	)	
Rate Regulation	)	

REPLY COMMENTS OF THE NATIONAL CABLE TELEVISION ASSOCIATION, INC. IN RESPONSE TO THE THIRD FURTHER NOTICE OF PROPOSED RULEMAKING

The National Cable Television Association, Inc. ("NCTA"), by its attorneys, hereby submits its reply comments in the above captioned proceeding.

I. The Commission Should Modify Its Proposed "Going Forward" Formula

NCTA's initial comments explained that the Commission's proposed methodology, by which rates would be adjusted if channels are added or deleted, contains significant drawbacks. We and many other commenters continue to believe that a mechanism that does not rely so heavily on the benchmark, and the slope associated with it, would be preferable in deriving rates for newly-added channels. But if the Commission adopts its preferred "going forward" methodology, NCTA urged that the proposed rule apply only on a "tier-specific", rather than a "tier-neutral", basis in order to limit what otherwise could be an excessive reduction in rates and to avoid problems that would be caused by rate changes for tiers to which programming services were not added or deleted. Many commenters raised this concern and pointed out that a tier- neutral

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approach would present serious disincentives to adding channels to regulated tiers.[1] We also agree with the suggestion of several commenters that the Commission's methodology be modified to allow cable operators to earn a reasonable return on their programming investments.[2]

The Comments of NATOA criticize the FCC's preferred going forward methodology as "unduly complicated."[3] But their solution is even more seriously flawed. Operators adding channels first would be required to return to the declining benchmark tables to recalculate their per-channel rates. The Commission, of course, has already tentatively rejected this going forward approach, understanding that it "would create substantial disincentives for cable operators with rates above the benchmark to add channels."[4] NATOA compounds these disincentives by also urging that operators undertake additional calculations to reduce their rates even further below the benchmark level for newly-added channels if they previously had taken external cost pass throughs or had per-channel rates lowered through a cost-of-service proceeding. This would present

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1 E.g., Comments of Cablevision Industries Corp. et al. at 8-9; Comments of Continental Cablevision, Inc. at 11; Comments of Time Warner Entertainment Co. at 3-5; Comments of Tele-Communications Inc at 2; Comments of Hearst Corp. at 4-8.

2 See Comments of the Disney Channel at 5-7; Comments of Cablevision Industries Corp. at 9-11; Comments of Discovery Communications, Inc. at 8-11; Comments of NBC at 4-6; Comments of Viacom at 9-10.

The Commission should also adopt the modification proposed in Newhouse Broadcasting Corporation's Comments in order to avoid penalizing systems with low rates and higher programming costs. See Comments of Newhouse Broadcasting Corporation at 3-4.

3 Comments of the National Association of Telecommunications Officers and Advisors, the National League of Cities, the United States Conference of Mayors, and the National Association of Counties at 15-16 (hereinafter "NATOA").

4 Third Notice at ¶ 138.

an additional deterrent to cable operators adding channels to a regulated tier. It would further penalize cable operators for taking wholly legitimate rate increases based on increases in external costs. NATOA's approach, in short, neither benefits from the administrative ease it claims nor serves the public interest.[5]

An additional problem with the Commission's proposal identified in our initial comments stems from the fact that under the Commission's rules, local governments could take up to four months before approving a going forward increase to basic rates. This regulatory delay will create enormous disincentives to the addition of channels to the basic tier of service. The New York State Commission on Cable Television suggests that "in order that the rules not deter cable companies from adding programming services to the basic tier, the Commission should consider a vehicle whereby the addition of channels would not necessarily be delayed for up to four months."[6] We agree. To facilitate the introduction of additional channels on basic service, the Commission should adopt the rule proposed in NCTA's initial comments: operators adding channels to the basic tier

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5 The Comments of Austin, Texas propose a wholly inappropriate modification to the Commission's "going forward" methodology -- that operators should be prohibited from obtaining increased rates where non-broadcast channels are added as a result of retransmission consent agreements between operators and broadcasters. Austin, Texas at 9. Austin, Texas purports to find support for this restriction based on the Commission's rule prohibiting pass throughs of retransmission consent fees for a year. The Commission in its Rate Order adopted this restriction based on its belief that "[c]urrent cable rates reflect the value of broadcast signals to cable operators." Rate Order at ¶ 155. This is surely not the case with respect to the addition of new channels of programming. Any programming costs and other costs, such as equipment and marketing, incurred as a result of carriage of new cable programming networks clearly are not reflected in the current rates charged and should not be discriminated against when the "going forward" methodology is applied to new channels of service.

6 Comments of the New York State Commission on Cable Television at 3.

should be permitted to implement a new rate upon thirty days' notice, subject to potential refund liability if the rate ultimately is determined to be unreasonable.

II. Recently Upgraded Systems with Rates Below the Benchmark Should Be Permitted to Raise Their Rates to the Benchmark

NCTA's initial comments endorsed the Commission's suggestion that cable systems with below benchmark rates who recently initiated or completed upgrades should be entitled to raise their rates to the benchmark level. Austin, Texas, however, claims that such a rule would give "special treatment" to some operators, and it should not, therefore, be adopted.

The Commission's approval is not special treatment but an effort to level an otherwise unlevel field. Freezing the rates of systems below the benchmark hardly results in equality of treatment for all systems. Rather, it penalizes those systems who intended to phase in rate increases. There is no reason to perpetuate this unfairness, just as there is not economic harm in allowing these systems to raise their rates to the presumptively reasonable benchmark level.

III. Operators Should Have a Choice Between Cost-of-Service on One Tier, and Benchmark on the Other

The proliferation of cost-of-service hearings is an outcome that neither the cities[7] nor cable operators desire. However, the cities persist in urging the Commission to require operators to make an either/or choice, the likely result of which, as the

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7 Indeed, NATOA proposes, at least for upgrades, that cost-of-service proceedings can only be invoked in the case of "special circumstances or extraordinary costs." NATOA at 8-9. Austin, Texas suggests imposition of a "mini" cost-of-service showing before an actual cost-of-service proceeding may be undertaken -- that is, an operator first must "make a threshold showing that benchmark rates do not enable [it] to earn a reasonable return on the overall system, including revenues from unregulated as well as regulated sources." Austin, Texas at 12.

Massachusetts Cable Television Commission's comments explain,[8] will be to increase the need for cost-of-service showings. While the cities may hope otherwise, cable operators whose costs make compliance with the benchmark rates impossible are not likely to be able to forgo recovery of those costs.

Franchising authorities primarily believe an "all or nothing" choice is necessary to guard against operators obtaining excessive returns. But as NCTA and many cable operator commenters in this proceeding explained, there is no need to impose a uniform rate-setting mechanism out of fear that operators will "game" the system. Adequate measures can be adopted to ensure that only a proper recovery is gained where a cost-of-service proceeding is undertaken on only a single tier.

If, however, the Commission adheres to its tentative decision to require a uniform rate setting mechanism, then rules must be adopted to avoid the need to make duplicative cost-of-service filings before two different regulatory bodies. NCTA and other commenters have therefore proposed that the FCC conduct a single cost-of-service proceeding.[9]

The Commission has years of experience in deciding cost-of-service issues, experience in which local franchising authorities are decidedly lacking. Most local franchising authorities, in fact, have no expertise in this area whatsoever. For this reason, the Commission should roundly reject the cities' suggestion that the FCC defer to their

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8 Comments of Massachusetts Cable Television Commission at 6 (expressing concern that "requiring a parallel approach will increase the number of cost-of-service cases before us (and the FCC).")

9 E.g., Comments of Cablevision Systems Corp. at 5-7 (FCC cost-of-service determination should be binding on local franchising authorities); Comments of Viacom at 17-19; Comments of Falcon Cable TV et al. at 18 (proposing operators have choice of seeking unified Commission proceeding); Comments of Joint Parties at 8 (FCC should make binding determinations on all significant ratemaking issues.)

cost-of-service findings.[10] Such deference would not only be unwarranted, but unlawful. The Cable Act simply envisions no role for franchising authorities in the regulation of non-basic cable programming tier rates. Indeed, it is the FCC which is to assume jurisdiction over basic rates, where the franchisor is decertified or otherwise unable to regulate the lowest tier. Franchisors should not be able to insinuate themselves into the expanded tier process reserved for the FCC through the guise of administrative simplicity.

IV. Franchise-Required Upgrades and Rebuilds Should Be Afforded External Treatment

Our initial comments and the comments of cable operators in this proceeding endorsed the Commission's proposal to permit external cost treatment for costs of upgrades required by local franchising authorities.[11] Such treatment is consistent with the rules governing pass throughs of franchise-required costs. A review of the franchising authorities' comments on this issue demonstrates that a rule allowing pass throughs of upgrades is also necessary in order to protect operators against cities' manifest hostility to allowing rate increases to cover these wholly legitimate costs. Operators should not be in a position where they are forced to undertake expensive improvements only to find that

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[10] Austin, Texas, for example, claims that "while it need not be binding, the decision by the franchising authority should be given considerable weight in the FCC's cost-of-service determination [on non-basic tiers]. The FCC would be entitled to (and should) rely on the franchising authority's determinations, as well as the evidence presented in the basic service proceeding, rather than duplicating the work." Austin, Texas at 11. NATOA urges that "[a] cable operator should be required to demonstrate compelling reasons to the franchising authority as to why it should not be bound by a rate decision by the Commission, and vice versa." NATOA at 14 (emphasis added).

[11] E.g., Comments of Cablevision Systems Corp. at 7-9; Comments of Continental Cablevision at 17-19; Comments of Time Warner Entertainment at 11-12; Comments of Tele-Communications Inc. at 9-10; Comments of Tele-Media Corp. at 6-8; Comments of TKR.

the franchising authority has judged such costs not to be recoverable in rates charged to basic subscribers.

For example, Austin, Texas argues that not only should automatic pass throughs be disallowed, but also that no increases are necessary because the benchmark rates already incorporate the costs of upgrades.[12] But there is no basis for this presumption. As Austin, Texas itself admits, "the benchmarks do not reflect the costs of a particular system. . . ."[13] Because the benchmarks are based only on number of channels, number of subscribers, and number of satellite-delivered channels, the Commission has explained that "[t]he current benchmark cannot directly determine rates for upgrades anymore than for other changes that do not affect the three variables already included in the benchmark, such as, for example, an upgrade of vehicles or increased wages."[14]

Given the previously identified flaws in the benchmarks, there is no reason to assume that they accurately reflect the rates charged by upgraded systems. Rather, they are based on the average rates charged by systems that have been deemed effectively competitive. It may well be that recently upgraded systems that are nonetheless "effectively competitive" charge above-average rates. And because the benchmarks capture rates charged at only a particular point in time -- a time that preceded the FCC's rate cap scheme -- an effectively competitive, upgraded system might have charged a higher rate on September 30, 1992 had it known future rate increases would be capped at inflation.

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12 Austin, Texas at 3.

13 Id. at 2.

14 Third Notice at ¶ 153, n.259.

Austin, Texas also claims that "system upgrades are often planned for years."[15] It therefore assumes that existing rates already include allocations for future upgrade expenditures. But this assumption, among other things, fails to take into account that under the benchmark scheme cable operator rates on regulated services have, in the main, been reduced by 10%. There is, moreover, no reason to presume as the Austin, Texas comments do, that effectively competitive systems have included the costs of future upgrades in their existing rates.

Finally, Austin, Texas also complains that pass-throughs would be complex. However, requiring operators to undergo a full-blown cost-of-service proceeding each time they wish to raise rates on account of upgrade and rebuild costs -- can one imagine a more burdensome solution for the operator and the franchisor?. It will subject operator investments to micromanagement by the cities, whose interests in keeping rates artificially low may well prevail over their interests in affording their subscribers the benefits of new and improved services. It is precisely to guard against that predisposition, and to ensure that the benefit of new channel offerings be available to customers[16] that all upgrade expenses should be treated as external cost pass-throughs, or the benchmarks should be adjusted to incorporate an upgrade "add-on"

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[15] Austin, Texas at 4.

[16] 47 U.S.C. §157(a) places the burden on parties such as Austin, Texas to justify schemes that would retard new technologies provided by cable.

CONCLUSION

For the foregoing reasons, and for the reasons set forth in NCTA's initial comments, the Commission should (1) modify its proposed "going-forward" methodology; (2) permit operators to rely on benchmarks to justify rates for one tier, and cost-of-service proceedings to justify rates on another tier; (3) allow below benchmark systems that have recently rebuilt or upgraded their system to raise their rates to the benchmark; and (4) allow external cost pass throughs of upgrade costs.

Respectfully submitted,

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